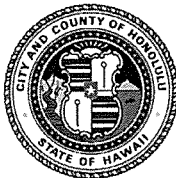


**OFFICE OF THE MAYOR
CITY AND COUNTY OF HONOLULU**

530 SOUTH KING STREET, ROOM 300 • HONOLULU, HAWAII 96813
PHONE: (808) 768-4141 • FAX: (808) 768-4242 • INTERNET: www.honolulu.gov

KIRK CALDWELL
MAYOR



EMBER LEE SHINN
MANAGING DIRECTOR

GEORGETTE T. DEEMER
DEPUTY MANAGING DIRECTOR

December 11, 2013

RECEIVED
CITY CLERK
C & C OF HONOLULU
2013 DEC 11 AM 9:22

The Honorable Ernest Y. Martin, Chair
and Members
Honolulu City Council
530 South King Street, Room 202
Honolulu, Hawaii 96813

Dear Chair Martin and Councilmembers:

SUBJECT: Proposed Resolution 13-292, FD1 -- Reaffirming the
City's Approval and Support of the Honolulu Affordable
Housing Preservation Initiative (HAHPI)

I regret to inform you that the introduction of Council Resolutions 13-291 and 13-292, relating respectively to the postponement or the rescission of the sale of the City's affordable housing projects to Honolulu Affordable Housing Partners, LLC (HAHP), has precipitated delivery upon the City of a Notice of Default from HAHP. A copy of the Notice of Default is attached to this letter.

You will note that the Notice of Default references a ten Business Days cure period.

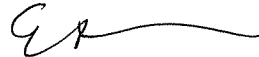
I am also attaching information about the financial impact that cancellation of the HAHPI sale would have on the City and the grants under the Community Development Block Grant program that were intended to be funded by the proceeds from the sale. This information was previously handed to you and/or your staff on Monday, December 9, 2013.

It is imperative that the Council immediately cure any alleged default and remove any cloud over the transaction by affirmatively stating - for the record - its support for the transaction and its intent to promptly introduce and enact a bill amending the City's leasing ordinance to extend the current March 31, 2014 deadline to close the City's transaction with HAHP.

The Honorable Ernest Y. Martin, Chair
and Members
December 11, 2013
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We therefore urge in the strongest possible terms that the Council, at its Wednesday, December 11, 2013 meeting, take up the attached proposed Resolution 13-292, FD1.

Very truly yours,



Ember Lee Shinn
Managing Director

Enclosure

cc: Councilmember Ann Kobayashi
Councilmember Ikaika Anderson
Councilmember Stanley Chang
Councilmember Kymberly Marcos Pine
Councilmember Carol Fukunaga
Councilmember Joey Manahan
Councilmember Breene Harimoto
Councilmember Ron Menor
Department of Community Services
Department of Budget and Fiscal Services

Honolulu Affordable Housing Preservation Initiative (HAHPI)
Financial Impact of Termination

TERMINATION EXPENSES		FY14	
Purchase & Sales Agreement			
Termination Clause		\$ 2,000,000	
City & County Honolulu Expenses			
Incurred to Date			
Legal		\$ 500,000	
Environmental		\$ 50,000	
Appraisal (12 @ \$25,000)		\$ 300,000	
Real Estate Broker Fees		\$ 50,000	
Total Incurred to Date		\$ 2,900,000	
Projected			
Potential Litigation, Fees & Costs		\$ 500,000	
Total Termination Expenses			\$ 3,400,000
OPERATING COSTS & CAPITAL EXPENDITURE			
Unbudgeted FY14 Operating Expenses			
Operating Deficit			
Debt Service & Maintenance		\$ 3,800,000	
Salaries & Wages			
Asset Mgmt (4 FTE @ 75%)		\$ 71,625	
CDBG Program Monitoring		\$ 37,500	
Legal Review and Counsel		\$ 37,500	
Asset Redevelopment			
Deferred Maintenance		\$ 900,000	
Total Unbudgeted FY14 Operating Costs & Cap. Expenditure			\$ 4,846,625
FY14 BUDGETED EXPENSES - Require alternate funding source			
Highway Fund			
Parking Revenues		\$ 408,000	
Other Post-Employment Benefits (OPEB)			
Fund Contingent Liability		\$ 26,000,000	
Program Income - CDBG & HOME			
Administration			
Salaries (18 FTE), grants management software, training and consultants		\$ 1,000,000	
Recommended Projects			
Housing First, Homeless Multi-Service Program Center, Housing, Shelter, Public Facility, Neighborhood Revitalization Strategy Area & Economic Development Projects; Public Improvement & Senior Housing		\$ 35,000,000	
Total FY14 Budgeted Expenses			\$ 62,408,000
OPPORTUNITY COST			
Commercial Tenant Settlement		\$ 500,000	
Asset Redevelopment			
Buyer proposed tenant and common area improvements		\$ 50,000,000	
Total Opportunity Cost			\$ 50,500,000
TOTAL TERMINATION IMPACT			\$ 121,154,625

NOTE: FY15 through FY18 Projected Annual Operating Costs & Capital Expenditure = \$12.9 MILLION

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC

745 Fort Street, Suite 1400

Honolulu, Hawaii 96813

December 10, 2013

NOTICE OF DEFAULT

VIA HAND-DELIVERY and CERTIFIED MAIL – RETURN RECEIPT REQUESTED
#7011 04701 0002 9591 2842

Department of Budget and Fiscal Services
Honolulu Hale
530 South King Street, Suite 208
Honolulu, Hawaii 96813

Attention: Mr. Nelson H. Koyanagi Jr., Director

Re: Honolulu Affordable Housing Preservation Initiative

Dear Director Koyanagi:

This letter constitutes a formal default notice which we are providing to you pursuant to and in accordance with the Purchase And Sale Agreement, dated October 18, 2012, as amended by that certain Restated First Amendment to Purchase And Sale Agreement, dated effective June 28, 2013, by and between City and County of Honolulu (the "**City and County**"), as Seller, and Honolulu Affordable Housing Partners, LLC ("**HAHP LLC**"), as Buyer, relating to the properties involved in the City and County's so-called *Honolulu Affordable Housing Preservation Initiative* (the "**Preservation Initiative Transaction**" or "**Transaction**"). The Purchase And Sale Agreement was executed by the parties after being approved by the City Council of the City and County of Honolulu by Resolution 12-228, FD1. (By Resolution 12-229, the City Council also approved execution of the ground leases, condominium leases, regulatory agreements, and other documents contemplated by the Purchase And Sale Agreement and/or incidental to the Closing of the Preservation Initiative Transaction.)

Thereafter, in preparation for Closing, HAHP LLC has expended or incurred around \$4 million in costs related to the Transaction. Under the terms of the Purchase And Sale Agreement, the Closing must occur by March 31, 2014. HAHP LLC has continued to move the Transaction forward and to advance the funds necessary to close the Transaction by March 31, 2014, in reliance on the City's commitment under the Purchase And Sale Agreement to close the Transaction by March 31 of next year.

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC

Mr. Nelson H. Koyanagi Jr., Director
Department of Budget and Fiscal Services
December 10, 2013
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Despite the City and County's express and implied contractual obligations under the Purchase And Sale Agreement to cooperate with HAHP LLC and not to undermine HAHP LLC's ability to finance and HAHP LLC's entitlement to close the Transaction, the Chairman of the City Council has recently, within the last few days, introduced two resolutions (Resolution 13-291 and 13-292) that will be formally considered by the full Council at its meeting this coming Wednesday, December 11, 2013, to rescind the Council's Resolution 12-228, FD1, approving the Purchase And Sale Agreement or to direct the City Administration either to postpone the Closing of the Preservation Initiative Transaction or cancel the Purchase And Sale Agreement. Under the terms of the Purchase And Sale Agreement, the City and County does not have the contractual or legal right unilaterally to rescind or cancel the Purchase And Sale Agreement or the unilateral right to postpone the Closing. By threatening to do so, however, and introducing and taking up for consideration and formal adoption separate Resolutions to terminate or cancel the Purchase And Sale Agreement or force a postponement of the Closing, the City and County has, whether negligently or willfully, undermined and made it impossible for HAHP LLC to finance HAHP LLC's acquisition of the properties involve in the Preservation Initiative Transaction. The City and County's actions in this regard constitute a violation and ongoing and material default of the City and County's express and implied obligations under the Purchase And Sale Agreement, including without limitation the obligation not to take actions to undermine and interfere with HAHP LLC's efforts to perform under the Purchase And Sale Agreement and to finance the Transaction. Aside from lost profits and other consequential damages suffered by HAHP LLC, the actions of the City and County, whether taken negligently or willfully, have had the effect of rendering completely worthless the \$4 million in costs that HAHP LLC has already invested into the Transaction. HAHP LLC estimated that it would incur an additional \$3 million to \$4 million in costs to close the Transaction, and, until the actions taken by the City and County, HAHP LLC was prepared to invest these additional amounts to secure the financing for the Transaction and prepare for Closing. It is incomprehensible that the City and County or a court would expect HAHP LLC to incur these additional expenses under the circumstances.

Pursuant to Section 8.1(b) of the Purchase And Sale Agreement, this letter will, therefore, serve as formal notice to the City and County that the City and County is in breach of its obligations under the Purchase And Sale Agreement for the reasons and in the respects stated above. In the event that such breach continues for ten (10) Business Days from the date of this letter, HAHP LLC shall be entitled to, and shall exercise, all of the remedies to which it is entitled under the Purchase And Sale Agreement and otherwise by law. Section 8.2(a) of the Purchase And Sale Agreement provides that, upon a default on the part of the City and County, and if HAHP LLC elects to terminate the Purchase And Sale Agreement, the City and County has authorized the Escrow

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC

Mr. Nelson H. Koyanagi Jr., Director
Department of Budget and Fiscal Services
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Agent to immediately release and return the Deposits and all interest thereon to HAHP LLC. Section 8.2(a) further provides that, in such circumstance, the City shall also be required to pay liquidated damages to HAHP LLC in the amount of \$2,000,000.

From the public record, it is our understanding that the Council Chairperson has introduced the proposed Resolutions because of concerns with the City Administration's plan for the expenditure of certain proceeds of the Preservation Initiative Transaction (approximately \$36 million) that would be considered "program income" under the Community Development Block Grant and HOME programs. Given this, we believe that, in addition to the \$2,000,000 in liquidated damages for which the City and County is liable under Section 8.2(a), the City and County is also liable for an additional \$500,000 in damages under Section 5.5 of the Purchase And Sale Agreement. Nothing in this letter is intended to waive any claim for additional damages that HAHP LLC has under Section 5.5 or any other provision of the Purchase And Sale Agreement in addition to HAHP LLC's claim under Section 8.2(a) of the Purchase And Sale Agreement. Further, while stating and reserving HAHP LLC's right to the \$2,000,000 in liquidated damages promised by the City and County pursuant to Section 8.2(a) of the Purchase And Sale Contract, our attorneys are researching whether the liquidated damages provision of the Purchase And Sale Agreement is binding to limit a party's recovery under a contract in circumstances where the other party to the contract negligently or willfully takes actions to defeat and undermine the performance of the aggrieved party; and HAHP LLC reserves the right, if supported by applicable law, to make a claim for the full amount of its damages, including consequential damages and lost profits, resulting from the City and County's breach of the Purchase And Sale Agreement.

In providing that a default must continue for a period of ten (10) days after written notice before such default constitutes a "default under this Agreement" and thereby entitles the aggrieved party to pursue its remedies under the Purchase And Sale Agreement, Section 8.1(a) contemplates that, in some circumstances, the defaulting party may be able to cure and avoid the consequences of the defaulting party's breach and default under the Purchase And Sale Agreement. Because of the timing of the City and County's default in this instance (at a crucial point when HAHP LLC needed to move ahead with its financing for a Closing no later than March 31, 2014), and because of the nature of the default (in which important and key officials of the City and County publicly announced a profound lack of support and commitment for the Transaction and the possible repudiation of the City and County's obligations under the Purchase And Sale Agreement), it is difficult to understand how the City and County might cure its default in this instance, whether within such 10-day period or otherwise. In the present circumstances, it would not cure the City and County's

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC

Mr. Nelson H. Koyanagi Jr., Director
Department of Budget and Fiscal Services
December 10, 2013
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default if the proposed Resolutions do not pass a vote of the full Council or are withdrawn. The negative impact on HAHP LLC's financing for the Transaction cannot be undone or reversed in time for a Closing by March 31, 2014. At this point, it is in fact difficult to understand how HAHP LLC's lenders could have any confidence or believe that the City and County, having once threatened illegally to repudiate its obligations under the Purchase And Sale Agreement, could be relied upon not to do the same again prior to Closing.

We deeply regret the action taken by the City and County. Under the Purchase And Sale Agreement, in addition to the proceeds from the Transaction payable to the City and County, we were committed to investing over \$40 million and actually planned to spend around \$50 million in rehabilitating the properties involved in the Preservation Initiative Transaction and to ensuring that many more units in the properties (about three times what was contemplated by the City and County's Request for Proposals) were set aside for low-income tenants. We firmly believe that we would have made valuable improvements to the properties and created better communities for the residents on a long-term basis. The actions taken by City and County have done more than simply render valueless our substantial investment in the Transaction and improperly undermine our ability to finance the Transaction. These actions have denied the families who live in these properties the improvements and security that would have been provided.

Sincerely,

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC
a Hawaii limited liability company

By **Highland Property Development LLC**
A California limited liability company
Its Manager and Member

By: 
William E. Rice
Its Authorized Manager

HONOLULU AFFORDABLE HOUSING PARTNERS, LLC

Mr. Nelson H. Koyanagi Jr., Director
Department of Budget and Fiscal Services
December 10, 2013
Page 5

cc: Department of Community Services
715 South King Street, Suite 311
Honolulu, Hawaii 96813
Attention: Director

Schlack Ito, LLC
Topa Financial Center
745 Fort Street, Suite 1500
Honolulu, Hawaii 96813
Attention: Carl J. Schlack, Jr., Esq.

Department of Corporation Counsel
530 South King Street, Room 100
Honolulu, Hawaii 96813
Attention: Gordon Nelson, Esq.

CBRE, Inc.
Pauahi Tower, Suite 1800
1003 Bishop Street
Honolulu, Hawaii 96813-3544
Attention: Scott B. Gomes

Via Email:
b.rice@highlandcompanies.com

Honolulu Affordable Housing
Partners, LLC
c/o Highland Property Development,
LLC
250 W. Colorado Boulevard, Suite 210
Arcadia, California 91007



RESOLUTION

REAFFIRMING THE APPROVAL AND SUPPORT BY THE CITY AND COUNTY OF HONOLULU OF THE HONOLULU AFFORDABLE HOUSING PRESERVATION INITIATIVE (HAHPI).

WHEREAS, as part of the City Administration's Honolulu Affordable Housing Preservation Initiative (HAHPI), it selected Honolulu Affordable Housing Partners, LLC (HAHP), through a request for proposals process, to purchase the leasehold interest in, and to renovate, a number of the City's low- and moderate-income rental housing projects (the "Projects"); and

WHEREAS, by adoption of Resolution 12-228, FD1, the Council approved a Purchase and Sale Agreement (PSA) between the City and HAHP to effectuate the City's leasehold sale of the Projects and the long-term lease of the land under the Projects to HAHP; and

WHEREAS, in adopting Resolution 12-228, FD1, the Council found that the proposed transaction contemplated by the PSA was in the public interest in that it: (1) would bring in a private-sector partner with the experience and capacity to manage the City's rental housing complexes into the future, (2) would provide for capital improvements that are needed to enhance the living environments for the Projects' residents, (3) would increase the number of rental housing units affordable to lower-income households earning less than or equal to 60 percent of median income, and (4) would provide for a substantial payment to the City that will be used for defeasance of City bond debt and for deposit into the City's CDBG and HOME program accounts; and

WHEREAS, the PSA provided for HAHP to make an initial deposit of \$1 million into escrow upon the effective date of the PSA and an additional \$4 million into escrow within two Business Days after HAHP's approval or deemed approval of the due diligence investigation authorized under Section 3.1 of the PSA; and

WHEREAS, Departmental Communication D-196 dated April 5, 2013 from Pamela A. Witty-Oakland, City Director of Community Services, stated that HAHP had made the required initial \$1 million deposit upon the PSA taking effect and reported that, as of April 1, 2013, HAHP's due diligence investigation of the



RESOLUTION

Projects had been completed and it had deposited an additional \$4 million into escrow; and

WHEREAS, upon closing, escrow is directed to transfer to the City, among other things, an “up-front lump-sum acquisition lease rent payment” of \$142 million; and

WHEREAS, escrow is scheduled to close on the purchase and sale of the Projects before March 31, 2014; and

WHEREAS, the benefits to be gained by proceeding to closing of the transaction are undeniable. These include: (1) the availability of proceeds to defease bond debt, to fund a rental assistance program for tenants, and to fund CDBG and HOME projects, including the City’s Housing First initiative, which offers the greatest opportunity to help the chronic homeless get off the streets and into permanent housing; (2) the funding by HAHPI of some \$50 million in much-needed improvements for tenants; (3) the preservation for the full 65-year lease term of the great bulk of the units as rental housing affordable to those at or below an income level of 60% of Honolulu’s median income, with affordable unit rent increases capped for the first ten years and with units thereafter remaining subject to regulatory agreements; (4) and the freeing up of City resources to focus on core City functions;

WHEREAS, the Council desires to convey its continuing approval and support for the HAHPI; now therefore,

BE IT RESOLVED by the Council that the City hereby reaffirms Resolution 12-228, FD1, which authorized the City Administration to enter into the PSA with HAHPI, and

BE IT FURTHER RESOLVED by the Council that the City hereby reaffirms its continuing approval and support of the HAHPI and the leasehold sale of the Projects and the long-term lease of the land under the Projects to HAHPI; and

BE IT FURTHER RESOLVED by the Council that, to further reflect the City's commitment to support the HAHPI and the leasehold sale of the Projects and the long-term lease of the land under the Projects to HAHPI, the Council hereby expresses the intent of the City to promptly introduce and enact a bill



RESOLUTION

amending the City's leasing ordinance to extend the current March 31, 2014 deadline to close the City's transaction with HAHP, in order to allow more time for HAHP to confer with its lenders and investors and to firm up the financing for the transaction; and

BE IT FINALLY RESOLVED that copies of this Resolution shall be provided to the Mayor, the Managing Director, Mr. Mark Chandler of the U.S. Department of Housing and Urban Development, and Honolulu Affordable Housing Partners, LLC.

INTRODUCED BY:

DATE OF INTRODUCTION:

Honolulu, Hawaii

Councilmembers